Components of a Farm Succession Plan

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Factsheet

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INTRODUCTION

Succession planning is a continuous process to plan for the transfer of knowledge, skills, labour, management, control and ownership of the farm business between one generation, sometimes known as the founder or retiring generation, and the next or successor generation. Succession is a process and not an event; it takes time and effort to work through and develop a comprehensive plan that best meets the needs of the farm family.

There are two main parts to developing a succession plan: (1) the "process" — discussing it, thinking about it, researching options, planning, deciding and (2) the "documentation" — recording the decisions through a written succession plan.

See OMAFRA Factsheet *Farm Succession Planning Steps and Checklist*, Order No. 10-025 for information on the planning process. This Factsheet deals with the components of a written succession plan.

MAIN ELEMENTS OF A SUCCESSION PLAN

A succession plan deals the transfer of three main areas:

- labour
- management and decision-making (control)
- ownership (the actual assets).

In most intergenerational farm transfers, the transfer of labour occurs first and is relatively straightforward. The transfer of management and decision-making, on the other hand, is not only the most difficult it is also key to the success of the entire process.

Management and decision-making transfer needs to be supported by a training and development plan. It will help to ensure that the next generation has the necessary knowledge and skills to take over and successfully operate the farm business in the future.

The transfer of ownership of assets involves the actual purchase/sale and/or gifting of the farm assets from one generation to the next.

Cost-share funding is available to help develop a succession plan through the Growing Forward Business Development for Farm Businesses Program. By participating in a Growing Your Farm Profits workshop and developing an action plan, farmers can access the following advisory services and learning opportunities:

- Farm Financial Assessment (supporting financial plan development)
- Agriculture Skills Development (supporting successor training and other skills development)
- Advanced Business Planning (developing a succession plan)
- Business Plan Implementation (help with some implementation costs such as legal documentation of ownership transfer)

Additional information about each of these can be obtained by calling OMAFRA at 1-888-479-3931 or at www.ontario.ca/growingforward. Applicants must meet the program eligibility criteria and adhere to all program terms and conditions and project claim submission deadlines to qualify for cost-share.

PRE-PLANNING ISSUES

Here are four issues that need to be addressed before preparing the written succession plan.

- Is the family goal to transfer the farm business to the next generation?
- If yes, then who are the successor(s)? Successors need to be part of the entire discussion and decision. Much of the initial work relates to this item. It focuses on opening the lines of communication, discussing the roles and responsibilities and defining each individual's personal and business goals and objectives.
- Is the farm business profitable and viable both now and in the long term? If the answer is no, then strategies need to be developed to address the short fall.

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- What is the implementation timetable.

If the family does not address these items as part of the process, then they may have challenges in completing the written succession plan outlined below.

COMPONENTS OF A WRITTEN SUCCESSION PLAN

A written farm business succession plan records and describes the decisions made about how the transfer of the three main areas will take place. While the format can differ, there are some common components:

- executive summary
- business overview
- strategic plan
- retirement plan
- management, control and labour transfer plan
- ownership transfer plan
- financial plan
- action plan and implementation timetable
- supporting documents

Although these next items may not apply in every plan, the following may also be needed:

- training and development plan for successor
- communication plan
- contingency plan

All these components need to fit together and create an integrated and comprehensive plan for the most successful transfer of the farm business.

DESCRIPTION OF EACH COMPONENT

A. Executive Summary

The executive summary is generally written after the succession plan has been drafted. It summarizes the plan and includes an overview of the current business, goals, strategies, action points and the timeline to implement the plan. The summary provides a quick scan of the plan without having to read the full document.

B. Business Overview

Similar to a business plan, it is useful to begin with an overview of the business that everyone involved understands and agrees upon. This includes points like:

- the size and location of the operation
- what the farm produces and how much
- who is involved in the business and in what capacity (e.g. makes decisions re genetics, cropping, etc.)
- the type(s) of business arrangement(s) (e.g. sole proprietor, partnership, corporation, rental agreements, etc.)

This sets the stage for the rest of the plan. It contains enough detail to provide a clear and concise picture of the business but is not overwhelming.

C. Strategic Plan

This component describes the business and personal goals and expectations of the founder (retiring) and the successor (next) generations in both the short and long term. It then lays out the strategies of how the business will meet these goals.

Discuss, clarify, address and define these goals and expectations first. Then write them down. This process makes sure everyone has the same reference point and ensures a clear understanding.

Once completed, the rest of the process and the resulting plan flow from it.

D. Retirement Plan

The retirement plan component deals with two issues — financial and lifestyle. It outlines what is going to happen in retirement (lifestyle) and how it will be financed.

Lifestyle considerations include desired activities for the retirees, how they will be involved in the business and so on. Part of this discussion addresses the living arrangements for the generations (i.e. who will live where).

The retirement financial component describes where the retirement money will come from (e.g. sale of the business, interest on savings, etc.), an explanation of any retirement-income strategies (e.g. RRSP's, RRIF's, LIR's, annuities, CPP, OAS, etc.) and how the money will be spent. Living and lifestyle costs are serious considerations at this point.

E. Management, Control and Labour Transfer Plan

This component describes how the transfer of management, control and labour (basically decision-making and workload) to the successor will take place. It also includes a timetable for this transition (see *Implementation Timetable, H*).

The abilities of the successor(s) also need to be closely connected to this component as the successor(s) must have the required skills and knowledge before the full responsibility can be transitioned to them. Consider including a component on *Training and Development Plan for Successor, J*.

F. Ownership Transfer Plan

The ownership transfer component outlines how the farm business is currently structured and how it will

change during the transfer process (see *Business Overview, B*). This includes a description of the intended business arrangement (e.g. sole proprietorship, partnership, corporation, etc.). Below is a brief example.

The farm is currently structured as a partnership with three partners. Under the plan, a corporation will be formed with three shareholders, each with an equal number of common shares. The non-real estate assets (cows, crops, supplies, machinery and quota.) will be rolled into the corporation. The individuals or partners will hold the real estate outside of the corporation. The corporation will then lease this farmland from the individuals or partners.

This component also explains how the transfer of asset ownership will be handled, including a description of the transfer mechanism (e.g. purchase, gift, bequest, combination, etc.).

For example, a sole proprietor plans to transfer the assets to the successor through the purchase/sale of individual assets (or a category of assets like machinery and equipment) over time with a mortgage back to the founders (parents).

Other parts of the ownership transfer plan component include:

- an explanation of the financing required, the various sources available and the preferred financing option(s)
- an inventory and valuation of assets and liabilities
- an explanation of the tax implications of the proposed transfer process along with a description of how these items will be addressed
- a discussion regarding the treatment of non-farming children
- an outline of the insurance requirements related to life, disability, disaster and related insurance tools
- a description of the legal agreements (e.g. employment contracts, partnership agreements, shareholder agreements, buy-sell agreements, etc.). Copies of these could be attached as appendices for reference purposes. It should be ensured that these legal agreements include dispute resolution mechanisms. A copy (or copies) of the legal will(s) and any prenuptial agreements could also be attached for reference.

G. Financial Plan

The farm business plan component of the succession plan describes how the farm business will meet the needs of both the retiree(s) and the successor(s).

This includes a financial analysis of the farm business — past, present and future — to determine if the business is profitable and viable. This is critical. If the business is not currently profitable and viable, then strategies need to be identified to make it so.

This component also describes the future direction of the farm business (e.g. maintaining the same scale, downsizing, expansion, diversification, value-added, etc.) and how this direction will affect the business and includes projected financial statements.

H. Action Plan and Implementation Timetable

This component provides a list of all the key activities to implement the overall plan and a timetable to complete them. These key activities need to be prioritized with deadlines (i.e. what must be done first and by when). This assists with monitoring and measuring progress. It also helps to identify if adjustments or amendments are needed.

I. Supporting Documents

Business and financial documents (e.g. mortgages, wills, financial statements) are necessary to obtain a complete and comprehensive picture of the farm business. Copies of these documents are gathered in this section for reference purposes.

OPTIONAL PLAN COMPONENTS

As noted, the following components may also be worth considering and adding to the succession plan:

J. Training and Development Plan for Successor

It is critical to ensure that the next generation has the necessary skills and knowledge to successfully operate a complex farm business.

This component of the succession plan then outlines these necessary skills and knowledge. This includes a current "skills profile" of the successor compared to a successful farm manager. Any gaps between these are then identified and an action plan of how to attain anything missing is developed.

A skills profile breaks down common farm activities into the required skills. For example, the capital purchases activity requires research skills, financial management skills, negotiation skills and so on. It might be identified that a successor lacks the negotiation skills.

This action plan may include such things as additional training, responsibility sharing, job shadowing and a multitude of other learning possibilities.

For example, continuing with the negotiation skills theme, an action plan might include the successor being authorized to negotiate small ticket purchases, such as farm inputs and as experience is gained, the authority would increase to make larger value purchases.

A performance review process may also be outlined under this component. This is a tool to give the successor feedback on how they are doing in their development. It helps identify both strengths and where improvements are needed.

The review process should be appropriate to the training and/or skills being acquired. For example, in a supervised training situation (i.e. learning to operate a specific piece of equipment), the review would be continuous (hourly or daily) with feedback. Moving across the spectrum from daily operations to delegated decision-making authority, the review would focus on the overall situation rather than continuous monitoring.

In all cases, regular meetings are important to review the successor's progress. They need to focus on what has worked, what has not, why and what could be done differently. This needs to be a two-way discussion and a positive experience for both the founder and the successor — a chance to share and learn.

Some of this discussion will look at technical production issues (e.g. feeding program, planting of a certain crop, etc.). It is also important to focus on management issues and responsibilities (e.g. purchasing decisions, financial management decisions, etc.).

K. Communications Plan

The communications plan has two basic parts:

- a description of how the family communicates about transition and succession planning
- a discussion of how disputes are managed and resolved

In the first part of the plan, it outlines the basic "rules" of family meetings, including:

- a schedule for regular "family business" meetings
- an outline of who will participate in these meetings (e.g. only those active in the farm business or all family members)
- if these meetings only involve those active in the business, should there be a separate "family" meeting for all family members
- where to meet and if meals will be involved
- an outline of meeting responsibilities and decision-making processes, such as who will set-up the meeting and agenda, follow-up on decisions, chairing meetings, etc.
- an outline of the ground rules (e.g. everyone has a turn to talk, not interrupting, no blaming, stay focussed on the agenda item, etc.).

The second part discusses how disputes will be managed and resolved. This might include such strategies as family voting, third party mediation, etc.

L. Contingency Plan

The contingency plan component outlines what will happen, and who will ensure the implementation of the contingency measures, in such situations as illness, death, disability, divorce, disagreement, disaster, business downturn or failure.

This includes reference to the insurance requirements and selected mechanisms particularly life, disability and disaster insurance as contingency planning and risk management tools.

OTHER RESOURCES AVAILABLE

OMAFRA Agricultural Business Management website at www.ontario.ca/agbusiness.

REFERENCES

Updated based upon: "*Growing Forward Business Development Program for Farm Businesses, Program Eligibility, Policy and Procedures*"

This publication is intended as general information and not as specific advice concerning individual situations. Although it outlines some of the legal and tax considerations of farm succession planning, it should not be considered as either an interpretation or complete coverage of the Income Tax Act or the various law affecting farm succession planning. The Government of Ontario assumes no responsibility towards persons using it as such.

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